



City Manager's Message

February 14, 2006

To The Honorable Mayor and Members of City Council:

It is my responsibility and privilege to transmit to the City Council the proposed Fiscal Year 2007 Operating Budget, and the proposed Fiscal Year 2007 - 2012 Capital Improvement Program. As I said in my first budget message last year, there is no more important duty for a City Manager than submitting a financially responsible budget that seeks to balance the community's needs for the services, infrastructure and facilities that only local government can provide, with the ability and willingness of residents and businesses to pay local taxes and fees. Ultimately, a budget represents the collective decision of the community, as expressed by Council actions, about what is most important for us to accomplish together, as well as how to finance those accomplishments.

I am proposing a \$503.5 million General Fund operating budget that is 7.0 percent above last year and that reflects a 6.8 cent real estate tax rate reduction. This budget is \$5.5 million below the \$509.0 million target established last November by City Council. It would allow a 6.8 cent real estate tax rate reduction. As required by the new budget process, I also am providing options for Council's consideration to reduce the fiscal year 2007 budget by an additional \$5.9 million to meet the alternative budget target of \$497.6 million. These options have been carefully considered. Although they are not painless, I believe they are reasonable ones to consider. If those options are chosen, the budget would grow at a 6.0 percent rate and further moderate the rate of growth in property taxes for every property owner by allowing an additional 1.8 cent real estate tax rate reduction.

The budget is shaped by a number of "budget drivers." Additional funds are necessary to maintain current service levels and implement or continue current City policies. Some of the main "drivers" of the budget are staffing compensation, transit subsidies, debt service, rent and facility maintenance, and grant match increases. The City must pay salaries and benefits that are competitive with neighboring jurisdictions and the generally tight job market in the Washington, D.C. area, or risk losing good employees. To do so, this budget proposes a 3 percent cost-of-living adjustment (\$5.7 million for City employees), and it proposes funding to maintain current levels of employee benefits for retirement (\$5.3 million), health benefits (\$3.0 million), and merit pay increases (\$2.8 million). The budget also provides \$2.5 million to maintain current transit service levels, \$1.7 million for debt service



increases, \$1.3 million for rent and facility maintenance cost increases, and \$1.1 million for grant match increases.

The School's budget faces similar "budget drivers" including a 3 percent COLA (\$3.9 million), increases in the cost of retirement benefits (\$3.6 million), and the cost of fuel and energy (\$0.7 million), and merit pay increases (\$3.5 million).

I have used the Council's Strategic Plan as a road map for making budget decisions. The revised Strategic Plan is printed in full at the front of the budget document. The budget is designed to be responsive to its priorities. We need to:

- Maintain and improve the quality of our neighborhoods, our business and shopping areas, as well as the physical environment in which we live, shop and work.
- Maintain and improve our infrastructure, such as road capacity, public transit systems, pedestrian and bikeways that we use to move about.
- Be good stewards of our environment and historic resources.
- Attract and retain employers and businesses, particularly small businesses, that both employ and serve our residents.
- Provide the social safety nets used to care for those in need and to remain a diverse and affordable community.
- Minimize the risks to life and property posed by crime, unsafe facilities, as we as are prepared to respond to emergencies.
- Provide for the education of our youth.
- Ensure a City government that is efficient, financially sustainable in the long run, and promotes a sense of community.

To meet these strategic goals, the budget includes additional funding to enhance services in a number of areas:

- An increase in our funding for gang prevention activities, including significant expansion of recreation programs targeted at teenage youth (\$239,000).
- The next phase of funding for the Charles Houston Recreation Center renovation (\$2.18 million).
- Other enhancements to public safety including: funding in the Capital Improvement Program (CIP) for a new E-911 call system (\$1.5 million), additional funds for Sheriff and Fire Emergency Medical Services operations (\$673,000).
- An increase in transit subsidies (\$2.462 million) to reflect the increased costs of supporting DASH, paratransit for the disabled and the City's share of METRO bus and rail operating costs, as well as \$6.415 million for the Metrobus and Metrorail capital



- program, and \$369,000 for DASH bus replacement.
- Increases in the social services area including: additional funding for a nurse for group homes (\$63,000) and a nurse for tuberculosis control (\$77,000), before/after school program coordination (\$101,000), increased grants to non-profits (\$125,000), additional funding for open space and affordable housing reflecting the increased value of 1 cent of the real estate tax due to increasing assessments (\$804,000 each).
- Increases in the CIP for site acquisition for a new Fire station (\$3.0 million), for preliminary work on the new Police Headquarters facility (\$4.84 million), and Holmes Run trunk sewer (\$3.0 million).

We are implementing the new budget process. Adopted by Council last May, the new budget process is designed to provide more time for City Council and the public to consider difficult budget choices. More importantly, the new budget process is designed to allow Council and the public to make more informed decisions about budget tradeoffs by providing more information regarding specific spending priorities. I understand that these priorities need to be weighed against the overarching need to moderate the growth in residential real estate taxes.

Last June I instituted internal budget process reforms to accelerate our schedule for preparing the budget, to produce a wider and deeper look at the operating and capital budget needs of the City, and to initiate a continuing improvement process to make our City's government more efficient and effective. I reported to you in depth on the status of these efforts last October at Council's budget retreat. Although much more remains to be done, the proposed budget you receive today represents the current results of those efforts.

The proposed City budget (excluding the Schools) would not increase more than that required to maintain current services and policies – about 6.4 percent. This budget requests only \$2.1 million in discretionary supplementals for City operations and proposes \$2.1 million in expenditure reductions through efficiencies or service reductions to completely offset those increases. City staffing levels would be maintained at essentially the adjusted FY 2006 levels with an increase of only 0.3 percent or 6.75 full-time equivalent positions.

The proposed operating budget for the Schools would increase by \$11.6 million or 8.4 percent. The proposed transfer to the Schools for operating expenses (including the cost of a 3.0 percent COLA of \$3.9 million) is \$150.4 million. This amount is \$1.8 million below the School's request and \$2.4 million below the target set by Council. The \$1.8 million reduction to the School's request represents only one



change – a lower assumption about the cost of health insurance premiums. Instead the budget has set aside that same amount in fund balance, and it would be available for Council to appropriate in case this assumption proves to be incorrect.

The School's request for capital projects is fully funded in the proposed budget with only one exception. I have reduced requested funding for a Minnie Howard Ninth Grade Center renovation and expansion in FY 2009 and FY 2010. The proposed CIP keeps that estimate at last year's approved CIP level pending further study of trends in construction costs and enrollment. This change reduces the School's request for Minnie Howard by approximately 50 percent or \$10.6 million.

I also want to express my appreciation to the Superintendent and the School Board for complying with our request for an earlier submission and for meeting the Council's proposed budget target.

In order to meet the lower, 6.0 percent growth alternative budget target established by Council, several options are proposed for its consideration. These are described in more detail in the budget overview, but in general they involve the following:

- Reduce the COLA to be provided to City and School employees from 3.0 percent to 2.5 percent (\$1.6 million).
- Reduce the proposed Capital Improvement Program in FY 2007 (by an additional \$3.8 million).
- Reduce the proposed Schools operating budget transfer (by an additional \$0.5 million).
- Reduce the proposed City's operating budget (by an additional \$1.2 million).
- Reduce the proposed designation in fund balance for School health insurance costs (\$1.8 million).

The impact on real estate taxes paid by Alexandria homeowners would vary depending on the budget options chosen by Council, but under either option Alexandria's tax rate would remain among the lowest in the region. The table below shows the variation in the tax rate, including the average increase in residential real estate taxes to be paid under the proposed budget and the alternative budget targets.



AVERAGE HOMEOWNER TAX INCREASE
(considers combined effect of increased assessments and decreased tax rate)

	If No Rate Reduction	Proposed Budget	Alternative Budget
Rate Reduction	0 cents	6.8 cents	8.6 cents
New Rate	91.5 cents	84.7 cents	82.9 cents
All Residences Average value \$526,852			
\$ change in taxes	\$786	\$427	\$333
% change in taxes	19.5%	10.6%	8.2%
Single Family Average value \$667,386			
\$ change in taxes	\$935	\$481	\$361
% change in taxes	18.1%	9.3%	7.0%
Condominiums Average value \$363,592			
\$ change in taxes	\$614	\$366	\$301
% change in taxes	22.6%	12.5%	11.1%

Although we do not yet know what tax rates our neighboring jurisdictions are going to consider, a real estate tax rate of between 82.9 cents and 84.7 cents is likely to remain among the lowest in the Northern Virginia region.

There are two targeted real estate tax relief programs and the budget sets aside \$4.15 million in funds for this purpose, a \$1.0 million increase or 32 percent increase over last year. I am fully aware that even with these significant tax rate reductions, the increased costs in real estate taxes due to increased assessments may be a hardship for some Alexandrian homeowners. This budget continues a targeted approach to provide more assistance to those low and moderate household incomes and the elderly and disabled. Last year, more than a thousand grants, averaging more than \$500 each, were given to low and moderate income homeowners to offset real estate taxes as part of the Affordable Home Ownership Preservation (AHOP) program. The budget sets aside an additional \$300,000 in fund balance to increase funding for this program. The budget also provides \$3.2 million real estate tax relief for the elderly and disabled, which will allow an increase in the income and housing value thresholds.



Only 11 to 12 percent of City employees actually live in the City, and it is difficult to compete with other public and private employers in the very tight regional labor market with only 2.9 percent unemployment. To maintain the City's ability to keep and attract a competent workforce, a number of budget adjustments are proposed. The proposed budget includes the cost of a 3.0 percent COLA for City employees (\$5.7 million), which is below the regional rate of inflation of 3.7 percent. It also includes merit pay increases for City employees (\$2.8 million), increased costs for payments to the Virginia Retirement System (\$5.3 million), and for health insurance premiums (\$3.0 million). Lastly, the proposed budget sets aside some fiscal year 2006 estimated surplus fund balance (\$4.0 million) for pay adjustments for general salary schedule employees and other needed adjustments to recover our competitive position vis-a-vis other major Washington metropolitan area jurisdictions. In response to new national accounting standards, I also have set aside \$1.5 million in fiscal year 2006 surplus fund balances to begin a process of funding the costs of our liability for future payments for retiree health benefits.

Through a careful review process I have been able to propose a decrease of \$6.7 million or 36 percent in the General Fund transfer needed for funding the Capital Improvement Program (CIP) compared to the prior year. The proposed CIP is designed to maintain, update and improve the publicly maintained infrastructure of the City. I strongly feel that we should not begin down a path that leads to the deterioration of our existing City office, recreational and school buildings, publicly owned historic properties, parks and open spaces, roads and transit systems, and sewers. However, the budget is able to reduce the need for debt service and cash capital payments that fund the CIP by designating \$7.4 million in estimated fiscal year 2006 surplus funds for this purpose, holding the growth in CIP expenditures in FY 2007 to the FY 2006 level, and reducing the need to borrow funds for the CIP in fiscal year 2006 – thus moderating the growth in debt service costs required in FY 2007.

During consideration of the fiscal year 2007 budget I have identified several longer range challenges that require future attention to assure the financial condition of the City is sustainable.

- The funding plan for the CIP contains \$24 million in unidentified funding sources to pay for a planned \$100 million CIP program in FY 2008. We will have to examine closely whether we can afford \$100 million in CIP expenditures in FY 2008, or whether we can use pay-as-you go financing or additional borrowing to provide the additional \$24 million needed to balance next year's CIP budget.



- We face future challenges in meeting competitive pressures of the regional labor market. Health care insurance costs for current employees are increasing at a rapid rate, and accounting standard changes are forcing the City to come up with a plan to fund its estimated \$80 million plus in liability for retiree health insurance benefits. We also must redesign the process by which we measure and maintain our pay and benefit competitiveness with other Washington metropolitan jurisdictions.
- The City is positioned financially to be ready for the coming slowdown in the real estate market. For future planning purposes I have assumed only a 4 percent growth in assessments next year. The City maintains a strong undesignated fund balance that could be used to absorb a sudden and unexpected downturn in the real estate market. We have the ability to adjust City spending by slowing down planned capital projects. And staff will closely monitor spending and revenues during the year so that we can pick up any negative trends in revenues or expenditures and make quick adjustments as necessary.
- Over the long range, the economic vitality of the City is the major determinant of the budget health of the City. The recent economic development summit has identified a large number of strengths, weaknesses, opportunities and threats to the future economic development of the City. It will be our collective challenge to identify the best course to follow to promote the future economic health of Alexandria's residents and businesses.

I have initiated several continuous improvement efforts to produce efficiencies and savings, improve the quality and timeliness of City services, and generally to challenge the status quo. I received a large number of suggestions for administrative process improvements from City departments. To date, we have acted on about a third of those suggestions I designated for follow-up, and we have the remainder under active consideration. As part of this process, I have established five key continuous improvement teams. They have been developing recommendations for me that will improve our personnel selection and hiring, training opportunities, purchasing systems and procedures, facility management and the composition and operation of our vehicle fleet. I also am following up on many additional department-specific suggestions for improvement and savings were identified in the budget process.



I have proposed a total of \$2.1 million in expenditure reductions in the budget. Among those are savings due to: the downsizing and the lengthening of the assumed life of certain City vehicles, trading used radio equipment to upgrade our current equipment, substituting DASH for more expensive METRO bus service, reducing overtime costs, reorganizing printing services, reducing temporary staff for human services, reducing the City's summer intern program, and reorganizing a section of Police administrative staff.

I have reviewed and updated a wide-variety of fees, fines and charges for services to bring them more in line with what is being charged by neighboring jurisdictions and to cover increased costs of certain operations. Some of these adjustments include: developer fees, code enforcement fees, refuse pick-up fees, ambulance fees, vendor fees for special events, marina boat-slip fees, and swimming pool permit fees. The budget also assumes the increase bus fares proposed by the DASH Board.

We have engaged several consultants to conduct efficiency and best practice studies in selected City departments. We also have hired a consultant to improve the City's use of performance measures for management and budgeting purposes. Also, we have joined with 28 other Virginia counties and cities in a consortium sponsored by the International City and County Management Association to collect and report on uniform performance data for the purpose of sharing and comparing best practices.

Finally, I want to thank Council, our residents, business persons and City staff for their suggestions on how to improve our City Services.

Sincerely,

A handwritten signature in black ink, appearing to read "James K. Hartmann".

James K. Hartmann
City Manager